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NEW BEGINNINGS
A GREENER AND MORE INCLUSIVE TRADE POLICY

■ **ELVIRE FABRY**
Senior Research Fellow, trade policy and Brexit, at the Jacques Delors Institute – Paris

This series is a cooperation between the Jacques Delors Institutes in Berlin and Paris and makes concrete proposals for the EU's next institutional cycle.

1 ■ A strategic policy under high tension

• Trade policy priorities will become even more strategic for the next Commission as the geopolitical dimension of trade policy is growing in importance. In the absence of clear foreign policy objectives, the Trump administration's trade policy will take precedence by default. Similarly, China's foreign policy remains primarily commercial. The ability of Europeans to keep the United States at the multilateral negotiating table and bring China back to it will be crucial for the systemic balance over the coming decades.

• The last legislative term has been a transition period for trade policy and marked the end of 'trade as usual'. In the wake of the negotiations for TTIP, strong internal challenges have emerged from civil society since 2014, as various actors intend to have greater influence over this policy area. Externally, unprecedented tensions between major trading powers have arisen since 2018. But a tightening of internal and external policy space foreshadows severe turbulence for the next Commission. In addition to the slowdown in world trade, which is amplified by the confrontation between China and the United States, there is a great deal of uncertainty about bilateral relations between the EU and the US, as well as the EU and China. The risk is a deterioration in these relationships that would necessitate a more defensive European position and mark a shift in the market access agenda. Moreover, the surge in support for the Greens in the new European Parliament and the need to strengthen the legitimacy of European trade policy call for an active 'greening' of trade policy, or the principles of openness will be seriously undermined.

• A reorientation of European trade policy has already taken place under the Juncker presidency. (for example, by ensuring greater transparency, promoting European standards through offensive bilateral policy, and developing a policy that 'protects without protectionism'). But there are blind spots that require changes in the current trajectory. In the face of Chinese state capitalism and the aggressive protectionism of Donald Trump, Europeans need to ensure that they can defend a globalisation with European characteristics that reinforces multilateral rules. In particular, trade policy issues will require more coordination between the various Commission Directorates General (DG), beyond DG Trade.

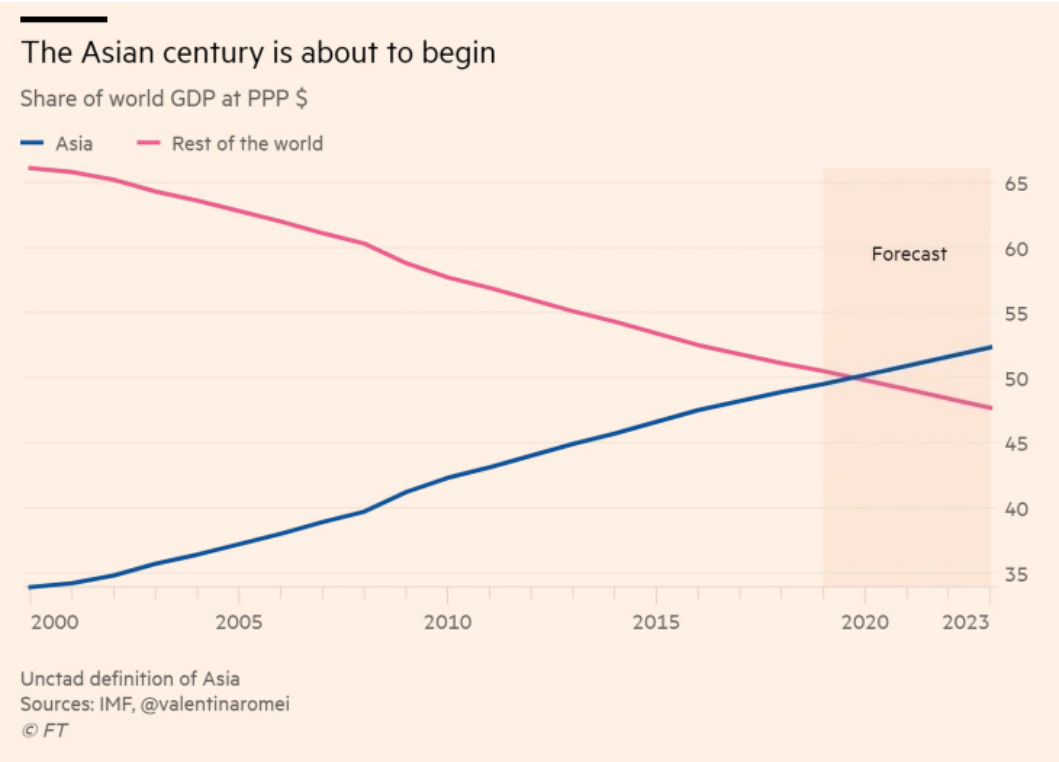
2 ■ Long-term challenges and short-term emergencies

2.1 The European trajectory of engaging in globalisation in the face of a new fragmentation of international trade

The EU is striving to maintain its position as the world's leading trading power through a bilateral policy of opening markets and promoting European standards. It has become more active in recent months as it seeks to take advantage of the disengagement of a protectionist America and in order to respond to the Chinese connectivity offensive (BRI), including in the digital domain. The ageing of the EU's population and stagnating domestic demand are driving the continuation of an aggressive trade policy that meets the appetite for consumption on other continents–not only in Asia but also in Latin America and Africa. Negotiations with various Asian countries are all the more strategic as Asia's weight in the world economy will exceed that of the rest of the world by 2020 as a percentage of GDP at purchasing power parity (PPP). The explosion of the Asian middle class is accelerating the region's economic integration and the shift in the centre of gravity of international trade towards Asia.

However, the EU also has to deal with the globalisation of market capitalism (removal of trade barriers, "made in the world", ever lengthening value chains, etc.) that seems to be coming to the end. The new American trade policy, based on protectionist isolationism and aggressive unilateralism, affects international trade all the more. Washington tends to sanction countries that do not engage in its campaign against China and is waging a cold trade war. But beyond the challenge of Donald Trump's re-election in 2020, deeper structural changes such as shortening value chains can be anticipated as offshoring costs have stopped falling for the first time since the early 2000s. While much of the growth in world trade will be in the services sector, service delivery remains dependent on geographical proximity. Moreover, a shortening of value chains would find support both in the United States and by some in Europe, as there has been a resurgence in demand for an identity-

FIGURE 1 ■



based economy, or economic nationalism. In addition to the two main economic actors, the state and the market, civil society now has a greater role to play in the conduct of trade policy. It mobilises both for a more active defence of global common goods (such as the fight against climate change) and for a more identity-based approach to production and consumption, which favours the circular economy and national preference.

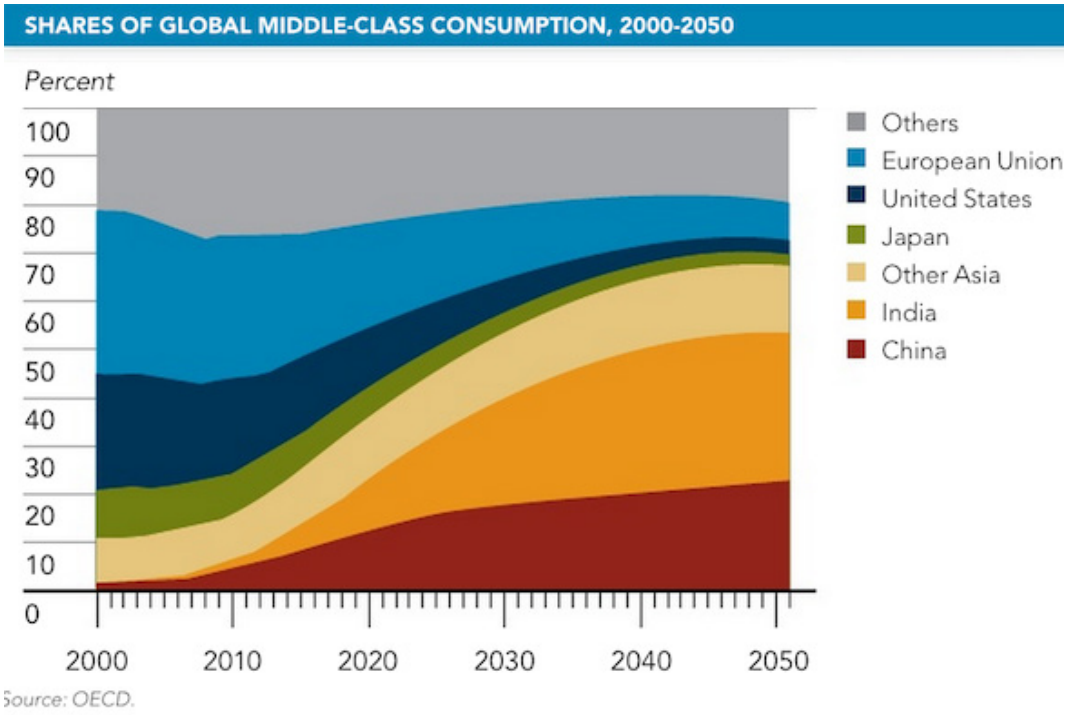
It is too early to conclude that economic disintegration, or *deglobalisation*, is taking place. Rather, at this stage, value chains are shortening at the regional level, which suggest a slowing of globalisation, a *slow-balisation*. But a growing role for identity and the geopolitical dimension of trade policy could accelerate the fragmentation of multilateral rules and lead to disengagement from international value chains. This would lead to more instability and conflict and limit European access to the demand of the global middle class, concentrated in Asia.

2.2 European leadership or isolation as a defender of multilateralism?

The EU is all the more defensive of multilateralism as the United States under Trump gradually disengages–to the point of threatening to block the functioning of the WTO Dispute Settlement Mechanism's Appellate Body at the end of December 2019. Moreover, the reality of Chinese trade distortions contradicts China's official discourse in support of multilateralism. The inertia of the West regarding the lack of Chinese convergence with common liberal standards since its entry into the WTO and the US blockage of WTO reforms in 2008 now call for an offensive policy to obtain guarantees for the reform of Chinese state capitalism as well as better anticipation of the rise of a protectionist India.

The weakening of multilateralism is significant. Since the early 2000s, the development of global governance has been

FIGURE 2



Source: OECD.

hampered by the rejection of rising powers to accept the liberal order that was designed by the West. While various rising powers that remain less open than the West are increasing their influence, the absence of an agreement between China, the EU, the US, which in turn lead the G20 process, is holding back the development of new multilateral rules. In addition, there is a global resurgence of protectionism. The United States and China are only responsible for a sixth of the increase in trade distortions that are attributable to all G20 members between the Buenos Aires Summit in December 2018 and April 2019. Many non-G20 countries have also doubled the use of restrictive measures (such as export subsidies and increased import tariffs) in spite of the G20 commitment to fight protectionism.[1] This makes the EU's leadership to forge coalitions of countries willing to defend multilateralism all the more complex.

2.3 The resurgence of economic sovereignty

The present geo-economic context is exerting strong pressure on a world economy that is dependent on international trade. Global interdependence and the specialisation of economic actors have become factors of vulnerability. The global slowdown in foreign direct investment reflects this. The new Commission must anticipate not only a shortening but also a risk of a breakdown of value chains. This could be fuelled by Washington's stated desire to apply sanctions more systematically, which would target both companies and third countries on the basis of national security criteria and the principle of extraterritoriality under US law. International dependence on the dollar makes value chains particularly vulnerable to US violations of multilateral rules. Retaliatory measures by trading partners, although legitimate, only exert additional pressure on value chains. The current debate on 5G infrastructure is indicative of the strategic challenges caused by European dependence on foreign subcontractors for key components of this infrastructure. At the dawn of the fourth industrial revolution, the challenge of access to rare earths, which are necessary to develop a number of technologies, encourages Europeans to better anticipate and ensure the conditions of their economic sovereignty.

2.4 A European liberalisation agenda with little consensus

The EU can only exert its full weight against the Americans and Chinese if it has strong cohesion between the capitals and citizen support. The commitment of the outgoing Commission to ensure greater transparency in bilateral negotiations, such as publication of negotiating mandates and position papers, and the strengthening of impact assessments for bilateral agreements, are key measures to restore public confidence. But these procedural changes are insufficient to address the criticism that European trade policy has an unequal impact on Member States, economic sectors and regions. Instead, a growing proportion of Europeans feel relegated to the periphery by this engagement with globalisation. Attention is also focused on the carbon footprint of trade. The outgoing Commission's shift towards a more inclusive and responsible trade policy (*Trade for All*, October 2015; *Managing Globalisation,* May 2017) has not been registered by citizens. The new Commission will have to commit to a more ecological trade policy, which addresses the urgency of combating climate change, protecting biodiversity and ocean governance. Its trade agenda will also have to be more inclusive.

Moreover, while the ability of a new generation of agreements that promote European standards among trading partners is crucial to rebuild political consensus

1. Jaw Jaw not War War. Prioritising WTO Reform Options, Simon J. Evenett et Johannes Fritz, CEPR, 2019, p6.

around European trade policy, the new Commission must also be more vigilant in ensuring that imports comply with European standards. It needs to quickly grasp the shortcomings and failures that exist in the compliance controls that are carried out by Member States, or this issue could soon become toxic for the legitimacy of European trade. The 'Schengen syndrome', a loss of confidence in the security of the external borders of the Single Market, could lead to a protectionist withdrawal. While companies focus on the lack of reciprocity in market access, citizens expect more protection from the EU and demand open trade that is accompanied by more safeguards.

3 ■ Key recommendations

3.1 Defend rules-based trade

In order to defend the legitimate objective to protect the environment, the new Commission must actively mobilise the full range of instruments authorised by the WTO as long as the damage caused to trade and the environment remains proportional and there is no discrimination in favour of domestic producers. All border restriction instruments would have to be adjusted in line with environmental objectives, such as quantitative restrictions on undesirable products, tariff incentives, and a carbon tax at the border. The same would apply to subsidies, such as restrictions on fossil fuels or fisheries and the development of ecological subsidies.[2] In line with Ursula von der Leyen's commitment to fight climate change, the Commission will only to be heard during this shift of European trade policy from trade liberalisation to regulated trade, if it adopts key measures that promote European sustainable development standards among its trading partners and ensures compliance in the Single Market:

• Make the granting of our trade preferences conditional on the ratification and compliance with the commitments of the Paris Agreement.

• Develop traceability of compliance with European sustainable development standards in the production methods of importers, placing the burden of proof with fundamental social and environmental requirements on importers and making compliance subject to sanctions.

• Commit to reducing emissions from maritime and air transport and strengthen multilateral initiatives (IMO, ICAO).

• Carry out an audit of customs authorities[3] in all Member States to assess the security and fiscal impact from deficiencies in control procedures and resources. Establish additional European capacities, such as European customs bodies financed (in part) by recovered customs duties.

3.2 Ensure more inclusive trade

• Establish a systematic evaluation of the cumulative sectoral, territorial and cumulative impact of agreements ex-ante and ex-post to ensure that the risks involved are properly anticipated and that the redistributive effect of these agreements on employment is better monitored.

• Replace the Globalisation Adjustment Fund with a European Transition Support Fund4 that is better endowed and would make it possible to take into account the combined effect of economic transitions, such as the restructuring of international trade, robotisation, as well as digital and energy transitions.

2. "Time to green EU trade policy; but how?", Pascal Lamy, Geneviève Pons, Pierre Leturcq, JDI, July 2019.
3. https://www.eca.europa.eu/Lists/ECADocuments/SR17_19/SR_CUSTOMS_EN.pdf
4. « Vers un fond européen d'accompagnement des transitions », Sofia Fernandes et Justine Daniel, JDI, 11 October2018.

3.3 Strengthen multilateral rules

• To overcome the deadlock of the WTO Appellate Body, the outgoing Commission's proposal to implement an ad hoc arbitration system, authorised by Article XXV of the Dispute Settlement Understanding,[5] will help to resolve an open crisis of multilateralism. But this option, which could only be temporary, would be limited in scope in a scenario where the United States isolates itself permanently and protectionism is increasing throughout the world.

• The EU's active engagement in establishing plurilateral coalitions, such as the EU-US-Japan plurilateral initiative to restrict subsidies and transfers of forced technology, would also be all the more necessary to promote the adoption of new multilateral rules. In addition to some key areas in which Europeans have a specific vision of globalisation to defend, such as storage and control of data (GDPR), sustainable development (e.g. the abolition of fossil fuel subsidies.), investment (i.e. the Multilateral Investment Court), the EU should also lead a multilateral initiative to safeguard access to rare earths.

• The dispute between Airbus and Boeing, which will continue with the reciprocal application of countervailing measures, should have prepared Brussels to better understand Beijing's growing competition in this sector. It should negotiate with Washington a framework for civil aviation subsidies and take this initiative to the multilateral level in order to set a precedent for strengthening WTO rules on subsidies in this specific area.

• To reduce asymmetries in market access and regulatory frameworks between rich and poor countries (for example on subsidies), the Commission should support a review of special and differential treatment by replacing the binary distinction between developed and developing countries with a graduation process. [6]

• To have an international impact at a time when services and digital regulations are being developed, the next Commission should actively complete the Single Market for services and accelerate the establishment of a European digital space at the same time.

3.4 A systemic approach to trade distortions that calls for better coordination of trade policy with other European policies (such as competition, research, and industry)

• In parallel with its multilateral commitment, the next Commission must put in place offensive measures to protect European interests and exert pressure on countries that maintain trade distortions. The major competition distortions threatening the EU are above all linked to the levers of unlimited subsidies to state-owned enterprises in some third countries. This issue requires the coordination of measures that will involve several Commission DGs and should start with:

• Adopting the international instrument on government procurement to ensure greater reciprocity with third countries and shift the burden of proof on foreign companies to ensure compliance with the WTO Agreement on Subsidies and Countervailing Measures.

5. « Sauver l'organe d'appel de l'OMC ou revenir au Far West commercial ? », Elvire Fabry et Erik Tate, JDI, 29 May 2018.
6. For the Many not for the Few: a Progressive Model for Trade and Investment, N. Benasconi & alt. FEPS, December 2018, p15.

• Promoting the use of the euro in international markets, including through bilateral trade negotiations, to anticipate a more systematic use of extraterritoriality by the United States.

• Implementing a global strategy for a level playing field that combines defensive issues (rapid implementation of the FDI control mechanism, identification of Single Market vulnerabilities–particularly in transport, customs or digital infrastructures–strengthening European competition policy to give it an external dimension) and offensive issues (such as European investment in disruptive innovations and the protection of strategic assets).

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PREMIER MINISTRE

Institut Jacques Delors
18 rue de Londres, 75009 Paris
info@delorsinstitute.eu – www.institutdelors.eu
Jacques Delors Institute – Berlin
Friedrichstraße 194, 10117 Berlin, Allemagne
info@delorsinstitut.de – https://www.delorsinstitut.de